ST. MARY'S UNIVERSITY

SCHOOL OF GRADUATE STUDIES

RISK MANAGEMENT AND SOCIAL PERFORMANCE IN MICRO FINANCE INSTITUTION IN CASE OF AGAR MICROFINANCE INSTITUTION (AMFI)

By Fantahun Abebaw

June, 2016

Addis Ababa, Ethiopia

RISK MANAGEMENT AND SOCIAL PERFORMANCE IN MICRO FINANCE INSTITUTION IN CASE OF AGAR MICROFINANCE INSTITUTION (AMFI)

By

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A thesis submitted to St.mary's university, school of graduate studies, in partial fulfillment of thesis requirement for the degree of Masters of Business Administration

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Acknowledgment

I would like to thank my thesis adviser Dr. Getie Andualem for his continuous follow up and advice. In fact without his continuous support it has been difficult to accomplish this research paper. I will forever appreciate the Agar microfinance institution staff for their cooperativeness.

Abbreviations and Acronyms

MFI	-	Microfinance institution
MIS	-	Management information system
MIV	-	Microfinance investment vehicle
AMFI	-	Agar microfinance institution
CSO	-	Credit and saving officers
SPM	-	social performance management

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Abstract

This study was aimed to recommend how managing risk used as a tool for promoting social performance of Agar micro finance institution(AMFI). For this research analysis we used the case of AMFI to show how improving risk- awareness of employees and their level of understanding of risk management could be used to achieve positive outcomes in terms of social performance of the institution. Obviously MFI risks are the potential for MFIs to deviate from their original social mission (social mission drift risk) explained as when MFI abandons its mission to serve the poor and starts lending wealthier people and the problem was observed similarly in the case AMFI . Hence the relationship between risk management and social performance were poorly justified on the basis of the role risk management indirectly plays in client protection in the case of AMFI. The general aim of this study is to recommend the use of risk management as a tool for improving social performance of microfinance institutions and the study would be valuable in promoting good social performance of AMFI been trying to ensure the institution do no harm to their stakeholders and maintain a good reputation of the trade. The study employed survey research methodology in which questionnaires were used. The study was also supported by the use of the CERISE Social Performance Indicators Tool (SPI4). Overall we found that the staff still needs to be equipped to understand why the risk assessment procedures are important. This study stands to justify good risk management practices can be used as a tool to improve social performance of AMFIs. Regardless of the argument the researcher observed a significant amount of respondents do not understand risk management used as a tool to promote social performance in AMFI. Due to those facts the researcher recommend AMFI should be optimistic to employ effective risk management practices as this will benefit all their stakeholders, particularly clients, through better social performance.

Key words*; - risk and social performance, high level of risk management awareness could be used to achieve positive outcomes in terms of social performance of the institution.*

CHAPTER ONE: INTRODUCTION

1.1 Back ground of the study

Early stages of the development of microfinance worldwide were characterized by microfinance institutions and other market players being greatly concerned about the financial performance of the retail providers. A lot of attention was given to financial performance, and issues regarding the sustainability of MFIs will be tabled for discussion and championed the world over. Social performance of MFIs received limited attention until disaster struck.

In 2010 over twenty microfinance clients in the Indian state of Andhra Pradesh committed suicide because they could not repay the loans they had borrowed and were under pressure from MFIs who were trying to recover the debts. Newspapers carried headlines like the following one that painted a dark picture of microfinance - “First they were stripped of their utensils, furniture, mobile phones, and televisions, ration cards and heirloom gold jewelers. Then, some of them drank pesticide. One woman threw herself in a pond. Another jumped into a well with her children. Sometimes debt collectors watched nearby (associated press,2012).

At about the same time a lot of criticism arose regarding microfinance's potential to reduce poverty. Stinging criticism came from authors like Bateman (2010) who argued that "microfinance was a major contributory factor in the destruction of the main positive economic and social development trajectories and in actual fact constituted a powerful poverty trap". Furthermore, a lot of criticism arose because of the massive returns that were being earned from commercialized microfinance. The darkness in similar fashion, an article published by Sriram (2010) at that time was entitled, "Microfinance: A Fairy Tale turns into a Nightmare". The sudden reputational crisis awoke the whole microfinance sector to the realization that neglecting social performance had the potential to completely destroy the trade. Social performance management has since then become a very important issue in the microfinance sector worldwide.

According to Gutierrez-Nieto et al. (2009) microfinance institutions have a dual orientation and their performance is assessed based on a 'Double bottom line', that is, 'Financial' (First bottom line) and 'Social' (Second bottom line). The second bottom line relates to the social mission of microfinance institutions. IFAD (2006) assert that the social value of microfinance relates to the manner in which the financial services provided improve the livelihoods of poor and excluded people. Social performance management helps to ensure that microfinance institutions deliver on their social expectations and effectively translate their social mission into practice (CGAP, 2007).

Existing literature to some extent portrays the relationship between risk management and social performance of microfinance institutions. Fernando's (2007) definition of microfinance risk includes the potential for MFIs to deviate from their original social mission. This risk is also noted by other authors who refer to it as social mission drift risk, social mission risk, or mission drift risk (Churchill & Frankiewicz, 2006; Churchill & Coster, 2001; Khan & Ashta, 2013; Abboushi et al., 2011). The term 'mission drift' otherwise refers to a phenomenon where a microfinance institution abandons its mission to serve the poor and starts lending wealthier people. The average loan size of the institution increases as wealthier clients crowd out the poor (Armendàriz & Szafarz, 2011; Christen & Drake, 2002; Dichter & Harper, 2007; Mersland & Strøm, 2010).

The relationship between risk management and social performance can furthermore be justified on the basis of the role risk management indirectly plays in client protection. Therefore we will like to investigate this relationship using the approach we employed.

1.2 Background to Agar micro finance institution (AMFI)

AMFI is one of the oldest MFIs in Ethiopia started operating in April 2004 as a non-profit making institution and is registered as a shareholding company. In addition to Addis Ababa the institution was operating in, Oromia & South nations and nationalities (SNNP) regional states of Ethiopia namely as at the time the study has been conducted. The founder shareholders of AMFI were 443 with a paid up capital of 4,243,600.

AMFI had six credit products at the time our study has been conducted and these were as follows:-

A. Micro business loan design for micro business operators and disbursed on group members guaranty ranges from 3 to 5 and individual bases. The loan size is up to birr 8000 ETB for the first cycle and increases as loan cycle increases. The maximum loan size disbursed is birr

25,000 through the loan term 18-24 months.

B. Small business loan is disbursed to licensed small business operator on individual bases .the loan term is for 24 months .Vehicles, House and Bank and Insurance certificate can be used as collateral for loan size above 20,000ETB. Whereas for loan amount up to 20,000 ETB salaried individual can be guarantor.

C. Construction loan is disbursed to those who need to undertake construction. To access this loan clients are expected to prove they under taking construction to their own house by presenting the necessary documents and generate sufficient income to repay the, loan.

D. General loan is loan product designed for salaried workers on group and individual bases. The loan size depends on the salary of employs and the loan term can prolonged up to 24 months with in three cycles.

E. Agriculture loan is designed to serve the farmer through branches outside Addis Ababa. The loan is only disbursed on group guaranty bases.

F. Women entrepreneur development program (WEDP) is designed to women clients in Addis Ababa. This loan is provided to female clients and the loan size is determined based on the cash flow of the business. The size of the loan can be up to birr 500,000.

AMFI uses both Group and Individual lending methodologies. In addition, the institution collects both compulsory and voluntary savings. The interest charged for the most common agriculture loan was a flat interest rate of 18% per annum. The loan has a term of one year. The only non-financial service provided by AMFI is in the form of training on small business management provided to their clients. The institution currently has 120 staffs out of which 61 are males and 59 are females. The institution's annual financial statements showed that as at 30 June 2015 (end of financial year); AMFI has a Gross Loan Portfolio of Ethiopian Birr 129.58milion accumulated savings/deposits of Birr 55.7 and has 10,141 active borrowers. The average loan size was Birr 12,777 and the amount of arrears was 3.19% of loan. The institution had earned a surplus of income over expenditure of Birr 20.53 million over the past financial year.

1.3 Problem statement

Early stages of the development of microfinance worldwide were characterized being greatly concerned about the financial performance of institution. A lot of attention was given to financial performance, and issues regarding the sustainability and Social performance of MFIs received limited attention in MFI in general and AMFI in particular. To support this, in 2010 over twenty microfinance clients in the Indian state of Andhra Pradesh committed suicide because they could not repay the loans they had borrowed and were under pressure from MFIs who were trying to recover the debts. Newspapers carried headlines like the following one that painted a dark picture of microfinance - “First they were stripped of their utensils, furniture, mobile phones, and televisions, ration cards and heirloom gold jewelers. Then, some of them drank pesticide. One woman threw herself in a pond. Another jumped into a well with her children. Sometimes the debt collectors watched nearby,(Associated press,2012). At about the same time a lot of criticism arose regarding microfinance's potential to reduce poverty. Stinging criticism came from authors like Bateman (2010) who argued that "microfinance was a major contributory factor in the destruction of the main positive economic and social development trajectories and in actual fact constituted a powerful poverty trap". Furthermore, a lot of criticism arose because of the massive returns that were being earned from commercialized microfinance. The darkness in similar fashion, an article published by Sriram (2010) at that time was entitled, "Microfinance: A Fairy Tale turns into a Nightmare". The sudden reputational crisis awoke the whole microfinance sector to the realization that neglecting social performance had the potential to completely destroy the trade. Social performance management has since then become a very important issue in the microfinance sector worldwide. Despite this obviously MFI risks are the potential for MFIs to deviate from their original social mission (social mission drift risk) explained as when MFI abandons its mission to serve the poor and starts lending wealthier people and the problem was observed similarly in the case AMFI . More over the relationship between risk management and social performance were poorly justified on the basis of the role risk management indirectly plays in client protection in the case of AMFI. In view of this, the researcher interested to assess the role of risk management used as a tool to achieve social performance in AMFI.

1.4. Basic research questions

This research have been intended to address the following issues in Agar micro finance institution (AMFI);-

1. How employs identify and manage institutional risks?
2. How employs understand the relationship between risk management and social performance?
3. How improving risk awareness of employees and their level of understanding of risk management could be used to achieve positive outcomes in terms of social performance?

1.5. Objectives of the study

The general aim of this study is to recommend the use of risk management as a tool for improving social performance of microfinance institutions. In addition to this, the study specifically address the following issue;-

- ❖ To determine employs awareness of institutional risk management?
- ❖ To determine employs understanding of the relation between risk management and social performance.
- ❖ To show how improving risk-awareness of employees and their level of understanding of risk management could be used to achieve positive outcomes in terms of social performance.

1.7 .Conceptual definition of terms

Social performance;- "the effective translation of an institution's social goals into practice in line with accepted social values; these include sustainably serving increasing numbers of poor and excluded people, improving the quality and appropriateness of financial services, improving the economic and social conditions of clients, and ensuring social responsibility to clients, employees and the community they serve".(CGAP 2007) .

Risk; - A risk is an exposure to the chance of loss.(Craig Churchill and Dan Coster risk management hand book 2001).

Risk management;- Risk management, or the process of taking calculated risks, reduces the likelihood that a loss will occur and minimizes the scale of the loss should it occur.(Craig Churchill and Dan Coster risk management hand book 2001).

Mission drift;- Mission drift in microfinance arises when an MFI finds it profitable to reach out to unbanked wealthier individuals while at the same time crowding out poor clients. (Beatriz Armend_ariz and Ariane Szafarz 2011).

CERISE Social Performance Indicators Initiative;- An analysis of internal systems and organizational processes determines whether institutions have the means in place to attain their social objectives(Zeller 2003).

SPI4;- Social performance indicator four, the Universal Standards SPM questionnaire in its current version helps financial service providers evaluate their level of implementation of Social Performance Management.

1.8 Significance of the study

According to IFAD (2006) the social value of microfinance relates to the manner in which the financial services provided improve the livelihoods of poor and excluded people. Social performance management helps to ensure that microfinance institutions deliver on their social expectations and effectively translate their social mission into practice (CGAP, 2007). Hence, the results of the study should be of great importance to the Agar microfinance sector in particular and micro finance sectors in general. Agar micro finance has been concerned about social performance management and been trying to ensure the institution do no harm to their stakeholders and maintain a good reputation of the trade. Similarly understanding an association between risk management and social performance would therefore avail other means of ensuring good social performance in AMFI. In addition, regulators and other concerned market players would therefore be able to ensure microfinance remains responsible by encouraging MFIs to implement strong risk management systems which will in turn improve the operations and social performance of the MFIs thus protecting consumers and other stakeholders. More over the result of the study may also be help full to other researchers as bottom line information for further study of this area.

1.9. Limitation of the study

The study encountered by three major limitations. The first limitation was inadequate financial resources. The second limitation was lack of time to administer all questioners through moving end to end at different branches of the institution. And finally the study limited by Unable to get Board of Directors to participate in the research because they were busy.

1.10. Delimitation of the study

Improving the level of understanding of using risk management as tool to address social performance issue is essential for financial institution. However, due to resource limitation this research proposal focuses on to assess the practice of risk management and social performance in AMFI. The study is trying to address the issue from credit and saving officers' (CSO) perspective at all branch of AMFI found in Oromia, Butagira and Addis Ababa. In addition to this the study is trying to address the issue from senior management perspective .we are preferring to undertake the study from CSO & senior managements' perspective because they are more prone to have understanding and knowledge about the practices of the institution risk management and social performance issues which are completely the concern of AMFI to maintain service reputation, so CSO have better understanding of risk management and social performance as far as they manage loan disbursement and repayment are likely supply accurate information. Finally the study will find out risks arise from loan products and the way how to manage such risks to achieve social performance mission.

1.11. Organization of the study

The remaining part of this paper were structured as follows: Chapter Two is the literature review section; Chapter Three explain the research methodology in greater detail; Chapter Four clarify data presentation and analysis and Chapter Five discus conclusions and recommendations from the study.

CHAPTER TWO-LITERATURE REVIEW

2.1 Introduction

This chapter reviews existing literature in the fields of risk management and social performance management. The first part of the literature review gives an overview of risk management in microfinance. This is followed by a discussion on the role of corporate governance in social performance management. The discussion extends to cover social performance management in greater detail and relates the practice to financial performance. The chapter also discus mission drift in MFI and the role of microfinance investors to assure social performance.

2.2 Risk Management in Microfinance

Micro Save(2009), define "Risk" as 'uncertainty of outcome that affects the objectives' that is a two-sided coin, on one side it has threat, and on the other it has opportunity. Risk is inherent to any business and microfinance institutions are no exception. What makes micro finance special is absence or near absence of traditional risk mitigation mechanisms like collaterals and guarantees. For example; Management of Credit Risk, therefore, becomes extremely important for micro finance institutions (MFIs). The monitoring, analysis and management of credit risk under group or individual lending models is core to the effective functioning of an MFI.

In the same vein, Fernando (2007) defines microfinance risk as "the potential for events or ongoing trends to cause future losses or declines in future income of an MFI or deviate from the original social mission of an MFI." He consequently argues that because MFIs have a social mission, mission drift is one of the major risks they are exposed to. Existing literature provides further support for Fernando's (2007) supposition of risks that are related to the social mission of microfinance institutions. Churchill & Coster (2001) identify social mission risk which they classify as a type of institutional risk. Likewise, Khan & Ashta (2013) identify mission drift and undeliverable social expectations which they classify as types of strategic risk. Moreover, Abboushi et al. (2011) identify social mission drift risk which they classify as an operations risk.

According to Micro Save (2007), there is near unanimous consensus that financial sustainability is a crucial gauge of the success of microfinance institutions (MFIs)—after all, an MFI that can cover its costs can also grow, serving more and more clients. Today, more than 400 sustainable institutions report to the Microfinance Information exchange (MIX), a leading source for market data. The industry as a whole is growing fast, adding 13 percent more borrowers each year since 1999.This growth is thanks in large part to the insistence on financial sustainability. But for most microfinance practitioners and funders, it is also important to reach poor and very poor people, to provide quality services, and most important to improve clients ‘lives. In other words both financial and social performance is positively affecting people’s lives. And the two aims are not necessarily at odds with one another. Thus, many funders and financial institutions are seeking more transparent ways to measure social performance in addition to measuring for financial performance. This Focus Note highlights the emerging emphasis on social performance in micro finance and reviews some of the assessment tools recently developed.

2.3 Categories of micro finance risk in the literature

The following literature presents the major types of microfinance risks and the table is composed from risk management frameworks designed by selected authors namely Churchill & Coster (2001), GTZ (2000), Abboushi et al. (2011), Goldberg & Palladini (2010) and Khan & Ashta (2013).

2.3.1 Institutional risk

Churchill and coster (2001) defined Microfinance success as an independent organization providing financial services to large numbers of low-income persons over the long-term. An assessment of risks against this definition results in three categories of institutional risk: social mission, commercial Mission and dependency.

A. Social Mission

While all MFIs do not have the same mission statements, in general they have a dual Mission: a social mission and a commercial mission. Their social mission is to provide valued financial services to large volumes of low-income persons that will enable them to improve their welfare. Microfinance institutions are vulnerable to social mission risk if they do not have a clearly defined target market and monitoring mechanisms to ensure that they are providing appropriate financial services to their intended clientele.

B. Commercial Mission

The commercial mission of MFIs is to provide financial services in a way that allows the Organization to be an on-going concern; that is, to exist for the long-term as a self-sufficient. MFIs are exposed to commercial mission risk if they do not set interest rates high enough to cover costs and if they are not managed as a business. The social and commercial missions sometimes conflict with each other. For example, offering larger loans might make it easier to become sustainable, but this could undermine the social mission to serve low-income and harder-to-reach people who traditionally demand smaller loans. The microfinance challenge is to balance the social and commercial missions to achieve them both.

C. Dependency

Dependency risk is similar to commercial mission risk, but it is most pronounced for MFIs Started and supported by international organizations such as CARE, particularly when the Microfinance activities are operated as a project rather than as an independent organization. These MFIs are vulnerable to dependency on support provided by the external organization.

2.3.2 Strategic risk

Strategic risks are commonly sub-categorized into Governance, Reputation and External business risks (GTZ, 2000; Goldberg & Palladini, 2010; Khan & Ashta, 2013). An interesting innovation in this area is the framework by Khan & Ashta (2013). They combine the GTZ (2000) framework with the list of 24 risk elements identified by the CSFI (2011) their 'Microfinance Banana Skins' report to obtain an expanded risk matrix for MFIs.

The part of Khan & Ashta's study that is important to our research is their identification of Mission drift and Undeliverable social expectations as risks.

Although Churchill and Coster clarify that**,** MFI managers and directors have less control over strategic risks, they should nonetheless assess the external risks to which they are exposed. A microfinance institution could have relatively strong management and staff, and adequate systems and controls, but still be prone to major problems stemming from the environment in which it operates. External risks are usually outside the control of the MFI, however it is important that these risks are perceived as challenges that the MFI should address, rather than excuses for poor Performance. Churchil and Coster categorized the following risks under external risks;-

A. Regulatory

Policy makers, banks and other regulatory bodies are becoming increasingly interested in, and concerned about, microfinance institutions. This concern is heightened when MFIs are involved in financial intermediation—taking savings from clients and then lending them out to other clients or institutions Regulations that can create vulnerability in an MFI include restrictive labor laws, usury laws, contract enforcement policies, and political interference.

B. Competition

In some environments, microfinance is becoming increasingly competitive, with new players, such as banks and consumer credit companies, entering the market. Competition risks stems from not being sufficiently familiar with the services of others to position, price, and sell your services. Competition risk can be exacerbated if MFIs do not have access to information about applicants' current and past credit performance with other institutions.

C. Demographic

Since most MFIs target disadvantaged individuals in low-income communities, micro finance managers need to be aware of how the characteristics of this target market increase the institution's vulnerability. In assessing demographic risks, consider the trends and consequences of illness and death (including HIV/AIDS), education levels, entrepreneurial experience, the mobility of the population, social cohesiveness of communities, past experience of credit programs, and local tolerance for corruption.

D. Physical Environment

Some areas are prone to natural calamities (floods, cyclones, or drought) that affectHouseholds, enterprises, income streams and microfinance service delivery. In addition, the physical infrastructure—such as transportation, communications, and the availability of banks in the MFI's area of operations can substantially increase its vulnerability.

E. Macroeconomic

Microfinance institutions are especially vulnerable to changes in the macroeconomic Environment such as devaluation and inflation. This risk has two faces: 1) how these conditions affect the MFI directly and 2) how they affect the MFI's clients, their business operations, and their ability to repay their loans.

2.3.3 Financial risk

Churchill and coster (2001) regrouped financial risks into;-asset and liability, inefficiency and system integrity risks.

A. Asset and Liability

The financial vulnerability of an MFI is summarized in asset and liability risks, which include interest rate, liquidity, and foreign exchange risks. **Interest rate risk;-** rises when the terms and interest rates of the MFI's assets and liabilities are mismatched. For example, if the interest rate on short-term liabilities rises before an MFI can adjust its lending rate, the spread between interest earnings and interest payments will narrow, seriously affecting the MFI's profit margin. MFIs operating in inflationary environments are particularly vulnerable to this type of risk. **Liquidity risk;** involves the possibility of borrowing expensive short-term funds to finance immediate needs such as loan disbursement, bill payments, or debt repayment. MFIs are most vulnerable to **foreign exchange risk** if they have to repay loans in a foreign currency that they have converted to local currency and therefore are earning Revenue in the local currency.

B. Inefficiency

Efficiency remains one of the greatest challenges for microfinance institutions. It reflects an Organization's ability to manage costs per unit of output, and thus is directly affected by both Cost control and level of outreach. Inefficient microfinance institutions waste resources and ultimately provide clients with poor services and products, as the costs of these inefficiencies are ultimately passed on to clients through higher interest rates and higher client transaction Costs.

C. System Integrity

Another aspect of financial management risk is the integrity of the information system, including the accounting and portfolio management systems. An assessment of this risk involves checking the quality of the information entering the system, verifying that the system is processing the information correctly, and ensuring that it produces useful report in a timely manner.

2.3.4 Operational risk

Operational risks are commonly classified into Transaction, Fraud, Legal & Compliance risks (GTZ, 2000; Goldberg & Palladini, 2010; Khan & Ashta, 2013). According to GTZ (2000) operational risks encompass poor information systems, human resources challenges, fraud and other operational problems.

Churchill and coster (2001) identify Operational risks are the vulnerabilities that an MFI faces in its daily operations, including Portfolio quality (credit risk), fraud risk and theft (security risk).

A. Credit

As with any financial institution, the biggest risk in microfinance is lending money and not getting it back. Credit risk is a particular concern for MFIs because most micro lending is unsecured (i.e., traditional collateral is not often used to secure microloans).To determine an institution's vulnerability to credit risk, one must review the policies and procedures at every stage in the lending process to determine whether they reduce delinquencies and loan losses to an acceptable level.

B. Fraud

Any organization that handles large volumes of money is extremely vulnerable to fraud, a vulnerability that tends to increase in poor economic environments. Exposure to fraud is particularly acute where money changes hands. These vulnerabilities in a microfinance institution can be exacerbated if the organization has a weak information management system, if it does not have clearly defined policies and procedures, if it has high staff turnover, or if the MFI experiences rapid growth.

C. Security

As with vulnerability to fraud, the fact that most MFIs handle money also exposes them to theft. This exposure is compounded by the fact the MFIs tend to operate in environments where crime is prevalent or where because of poverty, temptation is high. For example, in high volume branches the amount of cash collected on a repayment day can easily exceed the average annual household income in that community the management and board of a microfinance institution should consider each of the risks identified.

Table 1: summary of Microfinance Risks

1	Institutional Risks	Social Mission, Commercial Mission, Dependency
2	Operational Risks	Credit, Fraud, Security
3	Financial Management Risks	Asset and Liability Inefficiency System Integrity
4	External Risks	Regulatory Competition Demographic Physical Environment, macro economic

Source;- Churchill and Coster (2001) risk management handbook

2.4 Risks in Rural Microfinance

Goldberg & Palladini (2010) identify additional risks faced by rural microfinance institutions and classify them into Market risks, Production risks, Producer risks, and Climate risks. They categories Market risks into price volatility, irregular access to markets, poor infrastructure and inadequate information; and classify Production risks into land productivity, pests, disease and post-harvest risks. Producer risks comprise experience, technology and management ability; while Climate risks are broken down into drought, flood, wind, freeze, hail and heat wave.

Fernando (2007) argue that agricultural microfinance is risky because of the small farmers' exposure to natural hazards and the lower, volatile returns they get. A lot of agricultural activities require loans with longer repayment periods and less frequent installments because of the irregular cash flows small farmers receive.

2.5 Managing the Risks in Microfinance

Methods and practices for managing the various kinds of risk in microfinance have for a long time been the subject of research work and many recommendations exist in the literature. The following table that was adapted from Khan & Ashta (2013) summarizes the various risk mitigation measures in the existing literature.

Table 2: Survey of existing literature on risk mitigation measures

Risk	Mitigation recommendation	Source
Credit risk	Peer monitoring, group pressure, and social ties reduce delinquency	Al-Azzam et al. (2011), Armendàriz and Morduch (2010), Sharma and Zeller(1997)
	Frequent repayments	Armendàriz and Morduch (2010), Vogelgesang (2003)
	Public repayments	Armendàriz and Morduch (2010) Al-Azzam et al. (2011) Vogelgesang (2003)
	Choose more religious borrowers	Ahlin et al. (2011) Godquin (2004)
	Provide loans for productive purposes Go to rural areas (better group cohesion)	Armendàriz and Morduch (2010), Constantinou and Ashta (2011), Patten et al. (2001), Sharma and Zeller (1997)
	Disband older groups (as group age increases, repayment decreases)	Armendàriz and Morduch (2010), Vogelgesang (2003)
	Dynamic incentives (people who repay should be able to get new loans), long- term association	Godquin (2004), Sharma and Zeller (1997)
	Ensure that first repayments are not late, threaten to stop lending	Godquin (2004), Sharma and Zeller (1997)
	Do not increase loan sizes without appropriate screening	Constantinou and Ashta (2011), McIntosh and Wydick (2005)
	The provision of non-financial services (access to health and education) has a positive impact on repayment performance	Constantinou and Ashta (2011), Khan (2011), Quadri et al. (2011)

	Need for credit bureau Better information systems based on latest technologies Loan products should be tailored to client's cash flow Rescheduling of delinquent loans where the issues motivating delinquency could be resolved	Patten et al. (2001) Constantinou and Ashta (2011
Product risk	Great price differentials associated with risk	Constantinou and Ashta (2011)
Liquidity risk	Offer savings products	Constantinou and Ashta (2011), Patten et al. (2001), Paxton and Young (2011)
Market risk	MFIs should lend to entrepreneurs in domestic demand-based industries MFI activity should be in poor, un served areas or rural areas, even richer customers, especially in saturated markets	Patten et al. (2001) McIntosh and Wydick (2005), Patten et al. (2001), Vogelgesang (2003)
Portfolio risk	Diversify activity sectors within groups Diversify loan products	Sharma and Zeller (1997) Constantinou and Ashta (2011
Transaction risk	Better-educated staff, more training	Constantinou and Ashta (2011)
Fraud	Refocus incentives on collections	Constantinou and Ashta (201
Legal risk	Well-thought-out regulation reduces risk	Vogelgesang (2003)
Reputation risk	Have to collect, even reschedule to avoid contagion	Vogelgesang (2003
External business risk	Go to countries which are not too poor and not too rich Governments should develop a deeper financial sector Governments could increase	Ahlin et al. (2011) Ahlin et al. (2011) Al-Azzam et al. (2011)

	telecommunication access for borrowers Financially self-sufficient MFIs should co-exist with their subsidized counterparts, provided that these subsidies are carefully restricted to the poorest borrowers	McIntosh and Wydick (2005

(Source: Khan & Ashta, 2013 pp. 5)

2.6. Corporate Governance and Social performance in Micro finance

The growth of the microfinance sector worldwide and the strong support the field receives from donor organizations make it imperative that good measures be put in place to ensure donor funds are put to good use. Existing literature shows that corporate governance is widely regarded as one of the path ways to improving the efficiency of MFIs (Mori et al., 2015; Beisland et al., 2014; CSFI, 2014; Mersland & Strøm, 2009).

Mori et al. (2015) investigated the relationship between board composition and outreach or social performance using data from MFIs in East Africa. They argue that four aspects of MFI boards are important in improving outreach of MFIs. These are the independence of board members, nationality of board members, gender, and whether or not the members were part of the original founders of the institution.

Tchakoute Tchuigoua (2015) conducted a study to determine the elementary board characteristics that influence the quality of MFI governance using data from MFIs rated by Planet Finance. Tchakoute Tchuigoua found that the board attributes that determined the quality of MFI governance were: board expertise, board activity and ownership type.

Hartarska & Mersland (2012) examined governance mechanisms that promote efficiency in outreach of MFIs. They found that efficiency of MFIs increased in relation to board size up to nine board members and then declined afterwards.

Mersland & Strøm (2009) conducted a study showed that MFIs that had local directors as opposed to international ones, an internal board auditor, and a female CEO exhibited better financial performance.

Hartarska (2005) investigated the association between governance and outreach as well as sustainability of MFIs. They found that performance-based remuneration of management did not improve performance of the MFIs and that paying lower wages for MFIs with strong social missions was detrimental to their outreach

Barry & Tacneng (2014) examined whether shareholder-owned firms performed better than NGOs financially and socially using a sample from Sub-Saharan Africa. They found that NGOs were more profitable and had greater outreach than banks and cooperatives. Barry & Tacneng argue that poor rule of law favors socially-embedded institutions and Thus results in superiority of NGOs, but all the same banks may be pushed to serve more borrowers because of their stronger institutional quality.

Strøm et al. (2014) investigated the relationships between leadership, firm performance and corporate governance of MFIs. They found that female leadership was commonly associated with larger boards, younger organizations, being a cooperative or NGO, and serving more female clients.

Beisland et al. (2014) examined the relationship between microfinance rating scores and corporate governance and found that several of the governance metrics were related to performance of MFIs. Their results suggested that combining roles of CEO and Chairman was negatively associated with rating scores.

2.7 Social Performance Management

Micro saves social performance (SP) is as the ability of an MFI to the effective translation of an institution's social goals into practice in line with accepted social values‖3. This definition, which can be applied to all levels of performance in all operational aspects of an MFI, means that an MFI first should —*do no harm" &* second —is proactive in fulfilling its mission" (rather than assuming it will happen without action).

Micro Save's (2009) SPM is the effective translation of an MFI's social mission into practice by achieving certain goals/performance standards set out by the MFI itself, social performance management (SPM) focuses on: 1) setting clear objectives and creating a deliberate strategy to achieve them; 2) designing and implementing systems that are aligned with social objectives; 3) monitoring and assessing progress towards achieving the social objectives; and, 4) using social performance information to improve overall performance and decision-making. *Micro Save's* SPM is a client-focused approach that helps an organization to align its key systems with its mission, including Strategic Planning, Operations, MIS, Human Resources, Customer Service, Market Research, Product Development and Internal Audit and Control, thus helping the organization achieve its desired outcomes.

CGAP (2007) define social performance as "the effective translation of an institution's social goals into practice in line with accepted social values; these include sustainably serving increasing numbers of poor and excluded people, improving the quality and appropriateness of financial services, improving the economic and social conditions of clients, and ensuring social responsibility to clients, employees and the community they serve".

IFAD (2006) add that "the social value of microfinance relates to the way financial services improve the lives of poor and excluded clients and their families and widen the range of opportunities for communities".

Schellhorn (2012) assert that social performance management enables organizations to pursue and maintain their social mission in a self-regulatory manner and could be more efficient than external regulation because of benefits like increased staff motivation.
Thrikawala et al. (2013) highlight the importance of social performance measurements in that they are more aligned to organizational social and development goals, unlike other common performance measurements.

2.8. The relationship between Social Performance and Financial performance

A study by Hoepner et al. (2012) found that the relationship between social performance management and financial performance was in the form of an inverted U-shape. They argue that social performance management and social responsibility towards staff are important in order to sustain financial performance but their positive financial impact diminishes after a certain point. In addition, Hoepner et al. assert that although the initial costs of building clients protection systems can be very expensive, the efforts pay off once the "minimum critical mass" of client protection has been reached which ensures trust of clients and investors.

Meyer (2015) investigated the relationship between social and financial returns in microfinance. Their results provided evidence to suggest that MFIs with greater outreach to the poor also earned higher portfolio yields.

Guti´errez-Nieto et al. (2009) investigated the association between social and financial efficiency and found a positive albeit low correlation between the two. The results from their sample showed that save for one exception, there were no MFIs that were socially efficient but financially inefficient.

Adhikary and Papachristou (2014) investigated the relationship between financial performance and outreach of MFIs using data from South Asian countries. They found that breadth and depth of outreach were positively related to profitability and efficiency. Adhikary and Papachristou did not find any negative association between financial performance and outreach goals. They consequently argue that targeting poorer people is relatively less risky than pursuing greater numbers of clients and that it is possible for financially sustainable MFIs to achieve their social goals at an acceptable level of credit risk.

Servet (2011) makes a strong case for social responsibility in microfinance. He argues that it is wrong to simplistically assume that a negative relationship exists between financial performance and other performances (social and environmental) on the basis of additional costs alone. Better repayment of loans, customer loyalty, and lower transaction costs etc over-indebtedness.

Galema and Lensink (2011) assert that social investors in microfinance face a trade-off between, risk, returns and outreach. They postulate that there is a trade-off between returns and outreach because it is more costly to lend to very poor people.

In the same vein, Cull et al. (2007) investigated the association between financial performance and outreach of leading micro banks worldwide and found evidence supporting the possibility of earning profits while serving the poor.

Mosley and Hulme (2009) examined whether any negative association existed between growth and poverty alleviation in microfinance. Mosley and Hulme concluded that the adoption of design features that are significantly associated with good financial performance by MFIs (e.g. market interest rates and intensive collection of loan installments) could possibly increase their poverty impact and financial sustainability.

2.9. Mission Drift in Microfinance

According to Armendàriz and Szafarz (2011 mission drift as a phenomenon whereby an MFI increases its average loan size by reaching out wealthier clients neither for progressive lending nor for cross subsidization reasons. Thus, mission drift may arise because MFIs might find it optimal to reach out to wealthier individuals while at the same time crowding out poor clients.

Hishigsuren (2007) assert that mission drift does not result from deliberate intentions of an MFI but is instead caused by challenges from the scaling-up process. Hishigsuren therefore calls for MFIs to implement social performance management in order to prevent such mission drift.

In the same vein, Mersland and Strøm (2013) investigated mission drift claims because of criticisms that were being made against microfinance. Mersland and Strøm furthermore noted that the institutions' focus on serving poor clients did not change over time and thus concluded that the mission drift claims could not be confirmed.

Abrar and Javaid moreover claim that their results showed that profitability and risk were positively related to average loan size, while cost was inversely related to loan size.

Copestake (2007) reviewed the extent to which poverty oriented MFIs were able to use social performance management to prevent mission drift and to balance their social and financial goals.

Armendàriz and Szafarz (2011) postulate that mission drift is not driven by transaction cost minimization alone, but rather those poverty-oriented MFIs could potentially deviate from their mission by increasing their loan sizes for reasons that are neither progressive lending nor cross-subsidization.

2.10 Empirical Literature

❖ The 2010 suicide case of microfinance clients in the Indian state of Andhra Pradesh

The humiliating criticisms microfinance faced because of mismanagement and low social expectations that were never fully meet trigger microfinance institution to develop initiating policy. The 2010 suicide cases of microfinance clients in the Indian state of Andhra Pradesh were one shameful scenario that shed a dark shadow over microfinance this is because malpractices of microfinance institutions found in the region. For instance, during the time SKS microfinance posted profits up by 116 percent y-o-y (read: more than doubled), and also apparently held a secret board meeting .You don't need to be a Marxist to find a steep rise in profits disturbing for a microfinance which lost at least 17 of its clients to debt-driven suicide in the same year. Yet the crisis in Andhra Pradesh is far bigger than SKS and the five biggest MFIs — microfinance institutions — have realized this and collectively announced to restructure distressed loans. Finally, it took nearly two months of suicides, a heavy-handed regulatory clampdown and a media backlash to drive enough sense into the MFIs. The women's Self-Help-Group movement is also pushing for better regulation. How did we get here in the first place? .The poor are prone to debt traps. We must be aware that suicide in India is already shockingly common among farmers. But many, if not most victims in Andhra Pradesh were small traders, not subsistence farmers, so we're dealing with a new phenomenon here. It is no surprise that highly-indebted microfinance borrowers can be driven into debt spirals towards MFIs under conditions of heavy marketing, misinformation, social pressure to join self-help groups, and the vagaries of economic life at the bottom of the social order. If one thing goes wrong (an illness, a crop loss), an apparently sensibly invested loan suddenly turns into an insurmountable debt burden. In reality, "India Shining" is home to some of the poorest people in the world. Some micro financiers are apparently out of touch with this reality. Atul Takle of SKS went on the record telling the Associated Press, "I personally don't think a person would take her life for 225 rupees ($5.08) a week." But four out of five people in India live on less than 20 rupees a day (2007; latest figure I could find). As the dust settles in Andhra Pradesh, I predict that all these causes will be found. Webs of reasons will account for each suicide and will lead to complex fault-finding discussions; but it was the debt that pushed the debtors over the edge.

The same was the case for subprime borrowers in the USA who perhaps in some cases lost a job or fell ill, but never should have been granted the loan which brought them under an excessive debt burden in the first place (they were, however, lucky enough to find government assistance forthcoming).Therefore, financial markt regulators should act on alleviation of social risk resulting from poor risk management of microfinance institution.

2.11 The conceptual frame work

Conceptual frame work means concepts that related to on another were used to explain the research problem. Since effective risk management in micro finance directly related with good social performance management, AMFI should closely monitored risks to ensure strong measures are taken within the best time to either take advantage of the opportunity or combat the threats.

To align the conceptual frame work with the research objectives, risk and social performance in AMFI, depends on the appreciation of effective risk management could led to good social performance of the institution.

2.12. Conclusion

Social performance management partly arose out of the realization that because MFIs had a double bottom line - financial and social - they had to pay adequate attention to their social goals too. This is justified by the large amounts of donor funding they receive because of their social inclination (Guti´errez-Nieto et al., 2009; CGAP, 2007). The microfinance sector for some time ignored social performance and focused largely on financial performance only but some unfortunate incidents woke them up to the need to maintain their social goals. Top amongst these incidents were the strong criticisms the sector received after humiliating events like the suicide cases in the Indian State of Andhra Pradesh in 2010.

We have also discussed several issues in the literature that pertain to risk management and social performance management in microfinance. We managed to bridge the gap between these two disciplines by showing how risk management literature identifies some risks that are related to the social mission of AMFI.

Furthermore, some common risks that have long existed in risk management literature are also related to social performance. For instance, credit risk management plays an important role in preventing multiple-borrowing and ultimately over-indebtedness of clients which is a crucial matter in social performance management.

In the same vein, operational risk management encompasses maintaining effective information systems which is also crucial in preventing multiple-borrowing and over- indebtedness. In addition to this, governance risk is also directly related to social performance management as the board of director's play an important role in social performance management as was shown in the discussion on corporate governance. There for by considering risk management problems and the role of managing risks to improve social performance mentioned above, we will try to find out risk management and social performance problems in AMFI.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter presents a comprehensive overview of mixed method research and the research methodology used to conduct the study. It also discusses the data collection instruments used, the population and sampling procedures.

3.2. Characteristics of mixed method research

Mixed method research is relatively new as distinct research approach; it is useful to convey the collection, analysis of both quantitative and qualitative data in a single study. The researcher interested to use qualitative and quantitative research design because of its convenience to analyze both qualitative and quantitative data.

3.3. Research Methodology

The studies employed the survey research methodology. According to Visser et al. (2000) "a survey research methodology is a specific type of field study that involves the collection of data from a sample of elements drawn from a well-defined population through the use of a questionnaire". In the same, Susan E. Wyse (2012), argue that a survey research can be developed in less time, cost effective, relatively easy to administer and a broad range of data can be collected. The researcher employed a survey research methodology because it enables to extract detailed information with less time and cost effective to the study. In addition to the survey, the study was supported by the use of the CERISE Social Performance Indicators Tool (SPI4).

3.4 .Sampling design

Sampling provide a range of methods that enables one to reduce the amount of data needed for a study by considering only data from a sub- group rather than all possible elements. The target population of this study includes all credit and saving officer and senior managements in AMFI. Since the total population is manageable, the study did not involve any sampling as we choose to investigate all the relevant employees in the organization, which means a census approach was implemented. The organization employed a total of 39 credit and saving officers in the branches and 5 relevant senior managements at time of the study.

3.5. Sources of data

The study used both primary and secondary data, primary data was used for this study because it helps to answer specific research questions and data were current. Secondary data such as organizational profile, brochures and flying pamphlets had also been extensively reviewed as reference to supplement the gnarl back ground of the institution.

3.6. Data collection instrument

Primary data for the survey were collected using questionnaires. Two questionnaires were developed using standardized CERISE SPI Questionnaire used elsewhere, one for loan officers and another for management. Both questionnaires also contained a few social performance related questions in addition to the main risk management questions. Both of the questionnaires used comprised of a combination of close-ended and open- ended questions. The closed-ended questions were either presented on a Likert scale or were structured for respondents to choose “Yes/ No” responses. This was done in order to make the questionnaire easy to interpret and simple for the respondents to answer. The questionnaire could therefore be completed in less time. A few open-ended questions were however added in order to test the respondent’s in-depth understanding of some important concepts. Questions presented on the Likert scale asked respondents to indicate the strength of their agreement or disagreement with each statement on risk management on a five point Likert scale where: 1 = Strongly disagree; 2 = Disagree; 3 = Neutral; 4 = Agree; 5 =Strongly agree. We chose to use the Likert scale because it provides data that can be easily subjected to statistical analysis. In addition to this secondary data were collected from institutional brusher, fly pamphlet and organizational profile.

3.7. Methods of data analysis

To fulfill the objective stated data collection from respondents were coded and processed using SPSS statistical software. The data collected were analyzed using descriptive statistics with IBM SPSS statistical version .descriptive statistics used because the study was a survey research to know the opinion and feeling of respondents about risk and social performance in AMFI. The descriptive statistics was done using pie chart, tables mean and standard deviation.

3.8. Response rate for survey

A total of 39 questionnaires were distributed to all Credit and saving officers in the organization. AMFI employed a total of 39 loan officers at the time of the study and the officers were spread across the 10 branch offices the organization had. 36 of the questionnaires were returned. Three officers from a branch did not address the questionnaires and this accounted for the missing questionnaires. The response rate was therefore 92.3% which was reasonably good. This analysis was hence conducted using 36 questionnaires completed by the loan officers in the organization. The Management questionnaire was completed by 5 of the senior managers. Mangers they just were recruited and were therefore yet familiar with the study purpose.

3.9. Potential ethical issues

This research would benefit microfinance institutions in general and AMFI in particular by providing in-depth understanding of risk management and its controlling mechanism to achieve financial and social performance.

3.10. Validity and Reliability Test

Reliability refers to the extent to which the data collection techniques or analysis procedure will yield consistent findings. Cronbach alpha was used to the critical value of 0.70.the reliability measure for the dependability of the instrument to test for what it was designed to test was measured through acceptable scale suggest on Cronbach's alpha coefficient of construct is 0.6 (Bryman,2008),while a scale of 0.70 is preferable (swanson Holton,2005). In this research it is assumed that, if the test obtains the value of 0.60, it means the items in the model are understood by most of the respondents' .on the other hand, if the findings are far from the expected value 0.60, the respondents have different perceptions towards each item of the domain. For this research the reliability of 13 questioners were tested using cronbach's alpha and the findings showed that cronbach's alpha scale is 0.621, means that the questioners were understood by most of respondents.

Table,3 Reliability Statistics

Cronbach's Alpha	N of Items
.621	13

CHAPTER FOUR - DATA ANALYSIS AND PRESENTATION

4.1 Introduction

The findings of the research and analysis of the data collected were presented in this chapter. The SPSS and Microsoft Excel software packages were used to conduct the analysis.

4.2 Overall scores from closed-ended questions presented on Likert scale

Both the management and loan officers' questionnaires contained some closed-ended questions. Part of these were presented on a 5 point Likert scale that had options ranging from strongly disagree (1) to strongly agree (5). The remainder of the questions required that respondents choose one option from 3 pre-set responses: 'Yes', 'No' and 'Not sure'. The responses from the closed-ended questions that were presented on a Likert scale are analyzed below.

The first part of the analysis involved coming up with an overall risk management and social performance management score based on the questions presented using the Likert scale. This overall score would reflect the level of understanding of the issues possessed by each of the respondents. This analysis involved using the 'reverse-coding' Function in SPSS to transform the scale used for some of the questions that were presented on the Likert scale.

The questions were reverse-coded such that a respondent would get the highest possible score of 5 for giving the correct response to each question. Lower scores with a minimum of 1 would reflect inaccurate responses. Reverse-coding therefore permitted grading of respondents in line with the responses they gave such that respondents who answered questions correctly and could be deemed to have a high level of understanding of risk management and social performance had high scores on the scale. Results for management and loan officers are presented separately below.

4.2.1 Overall scores for Management

Questions 5 ,6,7,8,10,13,16,17 and 18 on the Management questionnaire were reverse-coded for analysis. This is because they had all been asked in a negative sense. A total of 15 questions had been presented using the Likert scale but Question 14 was omitted from the analysis because it had only sought to verify the level of competition in the microfinance sector and was not directly related to our analysis. Hence, the highest score that could be scored from the Likert scale questions was 70 (14 x 5). This highest score would reflect a respondent with the greatest sense of both risks Management and social performance management.

Table 4: Management's overall scores for questions presented on Likert scale

No. of respondents	5
Maximum possible score	70
Highest score	63 (90%)
Mean score	49(70%)
Lowest score	30(42.85%)
Std. Deviation	15.06 (21.51%)

Source; - own survey,2016

As shown on above table -3-the average score for the managers was 70% which was reasonably good. However, the standard deviation of 21.191 seemed a bit high suggesting that there were significant differences in the level of understanding of risk management and social performance principles amongst the senior managers. There appears to be a need for the organization to bridge this gap so managers reach a uniform level of understanding. This could be achieved through education and training.

4.2.2 Overall scores for Loan Officers

Questions 5, 6, 8, 9, 10 & 11 on the loan officers' questionnaire were reverse-coded for analysis since they had been asked in a negative sense. A total of 13 questions had been presented using the Likert scale, hence the highest score that could be scored from the questions was 65 (13 x 5). This highest score would reflect a respondent with the highest understanding of both risk management and social performance management.

Table 5: Loan officers' overall scores for questions presented on Likert scale

No. of respondents	36
Maximum possible score	65
Highest score	64(98.46%)
Mean score	40.73(62.66%)
Lowest score	14 (21.54%)
Std. Deviation	14.4(22.15%)

Source; - own survey,2016

As shown in the above table -4- average score for the loan officers was 62.66% which appeared good. However we have been observed on the above table, despite the standard deviation of the responses still appeared to be a bit high at 14.4. The range between the highest score of 98.46% and the lowest score 21.54% was quite wide and we have been affirmed wide gaps in the level of understanding of the loan officers that need to be addressed. Training would therefore be a useful tool in this regard.

4.3. Analysis of Likert scale questions appearing on both Management and Loan officers' questionnaires

We deliberately put some similar questions on both the Management and Loan officers' questionnaires in order to be able to analyze whether there would be any form of Association between the responses Management and loan officers would give to the questions.

4.3.1 Financial mission more important than Social mission?

This question was registered as question number (5) on the Loan officers' and it was posed as follows: "The most important objective for microfinance institutions is to meet their financial targets rather than Social goals ,a similar question again was put on the Management questionnaire as question number (6). We managed to evaluate personnel understood the need to balance between financial goals and social goals in Agar micro finance to this question. This is the sixth dimension of the Social Performance Indicators under the SPI4 tool. Of the 5 senior managers investigated 4 agree with the statement while 1 disagree with it .The responses received from the loan officers' are summarized below.

Descriptive Statistics

Table- 6: Summary of Loan officers' responses to question on importance of social mission.

	N	Minimum	Maximum	Mean	Std. Deviation
Q5.Social goals are less important than financial goals.	36	1	5	2.72	1.210
Valid N (list wise).	36				

Source; - own survey,2016

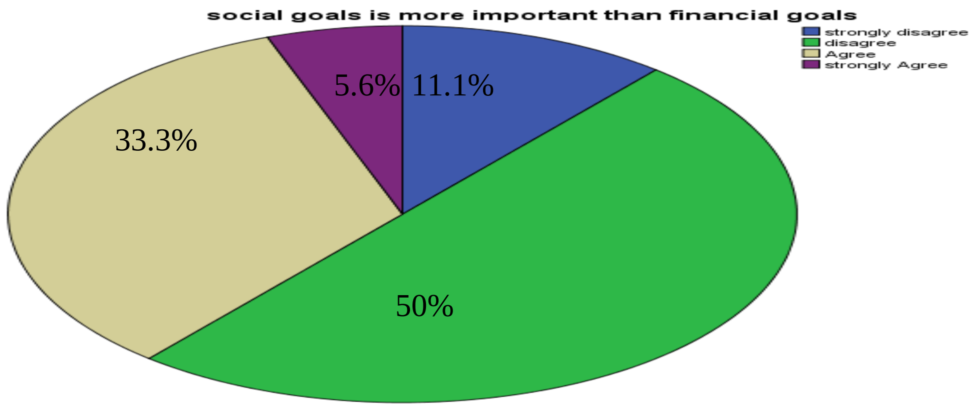

Figure -1: pie chart depicting Loan officers' responses to question on importance of social mission.

The mean for responses given by loan officers to this question was 2.72 which falls between points Disagree (2) and Neutral (3) of the Likert scale. This showed that on average the loan officers disagreed with the statement. However, as depicted in the pie chart above, 33.3% of the loan officers either agreed that social goals were less important than financial goals. Overall, responses from both management and loan officers showed that there was room to improve personnel's commitment to the social mission of the organization.

4.3.2 Over-indebtedness of clients is one of the major risks in AMFI

Question number (14) on the Loan officers' questionnaire and (9) on the Management questionnaire. It was presented as follows on the Management questionnaire: "Over-indebtedness of clients is one of the major risks faced by micro finance institutions".

Out Of the (5) senior managers, 1 strongly agreed, 2 agreed, 1 neutral and 1 disagree with the statement. The question partly tested the management how proactive with credit risks. The CSFI (2014) Microfinance Banana Skins survey reported that microfinance practitioners perceived that the over-indebtedness risk was the top risk face by the microfinance sector worldwide.

The responses received for this question from the Loan officers' questionnaires showed a mean response of 2.78 with a standard deviation of 1.017 as shown on table-5- and the pie chart below. The mean response was falls between points of disagree and neutral, since respondents were not certain about their agreement we can conclude that they disagree on this statement.

Descriptive Statistics

Table -7- summery of Loan officers' perceptions of whether over-Indebtedness was a major risk

	N	Minimum	Maximum	Mean	Std. Deviation
Q14. Over indebtedness of clients is one of the major risks faced by AMFI	36	2	5	2.78	1.017
Valid N (list wise)	36				

Source; - own survey,2016

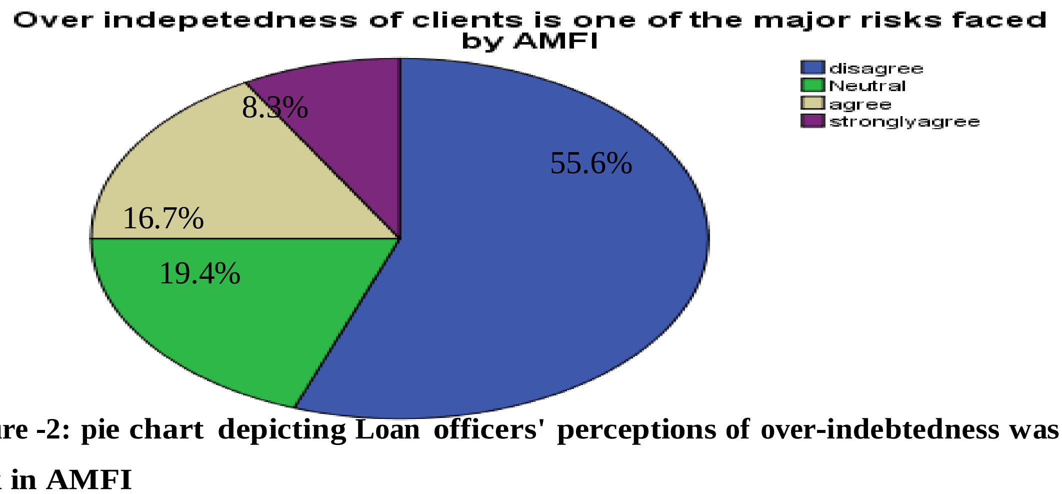

Figure -2: pie chart depicting Loan officers' perceptions of over-indebtedness was a major risk in AMFI

Most of the loan officers disagreed with this statement as shown by the mean response. Other factors held constant, the institution is loosely affected by over-indebtedness of clients.

4.3.3 Use of harsh and forceful debt recovery methods

It was question number (8) on the Loan officers' questionnaire and number (13) on the Management questionnaire. It was written on the Management questionnaire as: “using harsh and forceful methods are important to recover debts from clients”. 3 of the managers strongly on the statement while 1 agreed and 1 was disagreed. The question was to test the management's commitment of social performance management.

Descriptive Statistics

Table-8-summary of loan officer’s responses on using harsh and forceful methods is important to recover debts from] ,clients”.

	N	Minimum	Maximum	Mean	Std. Deviation
Q8.It is acceptable for AMFI to Occasionally use harsh and force full methods to recover debts	36	1	5	3.22	.797
Valid N (list wise)	36				

Source; - own survey,2016

The responses received for this question from the Loan Officers showed a mean response of 3.22 and standard deviation of 0.797 as depicted on the chart below.

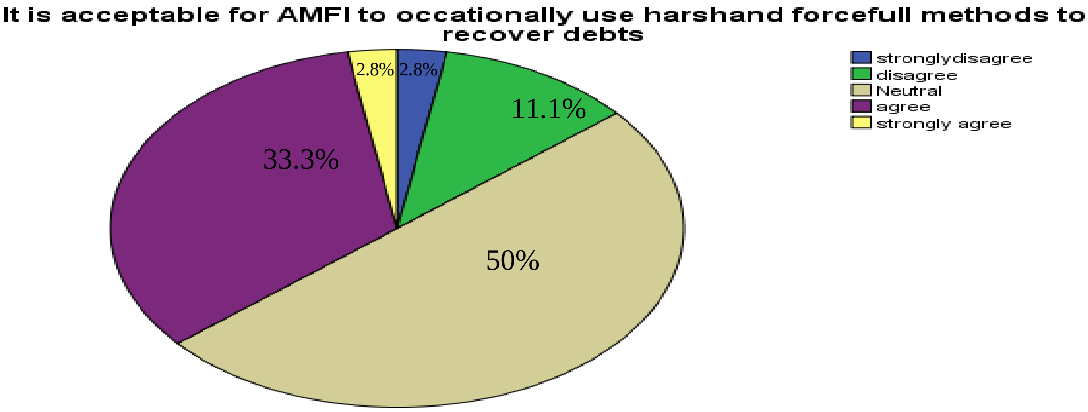

Figure 3: pie chart depicting Loan officers' responses to question on whether MFIs could use harsh debt recovery methods.

Although a significant proportion of the loan officers 50% choose one of the options neutral, 33.3% of loan officers were agree regarding the statement. Over all responses of managers and loan officers showed that the organization could be tolerant about the dangers of using harsh and forceful methods to recover debts.

4.4 Analysis of selected closed-ended questions on Management questionnaire

In this section analysis of selected closed-ended questions that were appeared on the Management questionnaire. The closed-ended questions comprised both the questions presented on the 5 point Likert scale and those that only required that respondents choose one option from 3 pre-set responses: yes, no and not sure. The responses given were discussed below;-

A. It is a great opportunity for MFIs to be able to lend to wealthier people since they are able to repay loans better (Que.5).

This question was intended to assess the management's knowledge and understanding of the concept of mission drift. As discussed in the literature review section, existing literature shows that mission drift is one of the major risks in microfinance (Beatriz Armendariz and Ariane Szafarz, 2001), “on mission drift in microfinance institutions” Management’s responses to this question are summarized in the table below.

Table 11: Summary of Management's responses to question on mission drift

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	2 disagree	3	60.0	60.0	60.0
	5 strongly Agree	2	40.0	40.0	100.0
	Total	5	100.0	100.0	

Source; - own survey,2016

As shown in the table Ten members of senior management were disagree that reflected the majority of management was familiar with the mission drift risk, However two members were agree for this particular statement. This showed that there was a gap on management understanding of mission drift which cover both social performance management and risk management functions of the MFI.

B) The role of Internal Audit in social performance management

On the management questioner question 29 & 31 sought to establish to assess Internal Audit function played a role in supporting social performance management. From the responses given for Que,29 only two(2) of managers replied their answer by saying "yes'', one manager replied by saying "No, and two managers replied by saying "Not sure". This showed that organization's Internal Audit is not very active in checking whether policies or procedures are correctly applied in the organization operations. There is therefore an opportunity for the organization to structure the Internal Audit function so it supports the social mission of the organization.

From the response obtained for Que .31, four senior managers replied by saying "Yes" and the remaining on manager replied by saying "Not sure".

This indicate that even though AMFI's internal audit or other departments visit systems annually to check whether complaints made by clients satisfactorily resolved the departments were reactive for problems to be resolved .there for there is a room for the organization internal audit continuously monitor to ensure policies and procedures correctly applied.

4.5 Analysis of open-ended questions on the Loan officer's questionnaire

These section analyses responses received for selected questions on the management and loan officer's questionnaires. The responses are discussed below under the respective questions.

A. Awareness of loan officers on organizational risk

Question 28 includes three questions (a, b, c), of their questionnaire asked that to identify the three major risks they thought the organization was exposed. The objective of the question was not only to see whether the loan officers could correctly identify risks the organization was exposed but also to test their ability to correctly name any kinds of risk was to some an extent an indicator of their knowledge of risk management principles.

Out of 36 loan officers, 12 (33.33% was able to correctly identify only 1 kind of risk (credit risk), 8 (22.22%) was managed to correctly identified 2 kinds of risk (political &market risk) while only 5 (13.9%) of respondents managed to identify three risks correctly (credit, markt, operational risks). The remaining 11 (17%) percent of the respondents failed to identify risks correctly. The finding showed that the staff had very limited knowledge of risk management as the field was required some understanding of risks to answer this question correctly.

B. Loan officers understanding of the method used to assess credit risk

An open-ended question number 29&30 requiring respondents to describe methods used to assess credit risk before and after lending was included in the loan officers' questionnaire.

Regarding this statement only 36.1% of the loan officers (13 respondents) managed to explain the pre-lending credit risk assessment procedures clearly and most of them understood that they were required to continue monitoring borrowers after lending. Loan officers' credit risk assessment skills were further tested by two more questions (31&32) and sought to establish whether they prioritized group guarantees or physical collateral over the viability of business ventures when lending. For these questions, 80.56% of the loan officers (29 respondents) understood the importance of individual ability and business engagement as a priority to offer loan and group guaranty and physical collateral.

Comes later while 11.11 %(4 respondents found it adequate to have group guarantees and the remaining 8.33 (3 respondents) to have physical collateral. Overall, although it is clear the organization has good documented procedures for assessing credit risks, it seems there is a gap in implementation of the procedures. The organization has to ensure that sound understanding of credit risk management procedures is instilled in the loan officers. This could be done through risk management training exercises.

4.6 Summary of results from the CERISE SPI4 tool

4.6.1 Results for Universal Standards for Social Performance Management.

In this universal standard score there are six dimensional tools to measure organizational social performance implementation discussed below;-

A) Dimension -1 Define and monitor social goals

Under Standard score 1a which required that the institution to have social strategy to achieve Its social goals we found that there was room for the institution to improve as their strategy did not define social goals comprehensively enough. In addition, the strategy did not adequately define measurable social targets for client-level outputs and outcomes.

Under Standard 1b which required that the institution collect, report, and ensure the accuracy of client-level data that are specific to the institution's social goals, there was need for the institution to comprehensively collect data for their social goals as well as MIX social performance data. Furthermore, there was need to consistently monitor the poverty levels of clients. This can be achieved through poverty out of poverty index (PPI).

B) Dimension 2- Ensure Board, Management and Employee commitment to social goals

Under Standard 2a which required that members of the board of directors hold the institution accountable to its mission and social goals, to consistently review more comprehensive social performance data.

C. Dimension -4-Treat Clients Responsibly

Standard 4a support that the prevention of over-indebtedness of clients, the institution's internal audit department needed to adequately monitor whether policies to prevent over-indebtedness of clients were applied. The finding showed that the internal audit was apparently limited to annual visit of client and passive actors for observed problem in the operation process. Furthermore it was not very active in social performance management.

D. Dimension five treat employs responsibly

This dimension supports the need to adopt policies to ensure the health and safety of employees. The organization could conduct the employee satisfaction surveys on an anonymous basis whereby employees can provide feedback without informing their self. This will have positive impact for the organization.

4.7. Conclusion

This chapter presented the findings from the research study. The next chapter presents the Major conclusions and recommendations made from this study.

CHAPTER FIVE- SUMMERY, CONCLUSIONS AND RECOMMENDATION

5.1 Summary

The study had intends to prove that there was an association between risk management and social performance, this implies that good risk management practices and the presence of risk awareness in AMFI employs would be associated with good social performance of the institution.

Overall we found that the staff still needs to be equipped to understand why the risk assessment procedures are important. This would be more beneficial than a situation where staff implement procedures without an understanding of why that is done. In addition the organization needs to gain an understanding of risks that are associated with social performance as these pose great threat to the organization as it is has to uphold the social mission.

As mentioned in the introductory chapter the second phase of our study showed the organizations alternatives to improve social performance management. The study implement SPI4 tool to identify gaps in social performance management in the institution and the results showed that there was a room to improve social performance management in the institution.

5.2 Conclusions

5.2.1 The relationship between risk management and social performance

The Researcher believed that good risk management practices can be used as a tool to improve social performance of AMFIs. Regardless of the argument, most of the time staff and management do not pleased about the risks the MFI is exposed to; the argument is similarly as observed in AMFI as a significant amount of respondents do not understand risk management used as a tool to promote social performance. This is because the institution would consequently fail to manage risk exposures that could result in harm being suffered by either the clients of the institution or other stakeholders. Ultimately, because the risk exposures are not managed, AMFI could unconsciously cause harm to its clients or stakeholders because the institution does not manage risks and this would be associated with poor social performance.

5.3 Recommendations

5.3.1 Implementing risk management and the provision of risk management training to staff

Giving emphasis to our area of study, AMFI, we found that a risk management practice in AMFI was a recent practice. This was manifested by only one risk officer appointed at head office level; as a result it would not be fully functional. We therefore recommend that AMFIs should make necessary investments in staff in order to improve their risk management functions. This could be achieved through hiring qualified employ in the field or by providing continuous enterprise- wide risk management training.

5.3.2 Commitment of the management and staff to social goals

We recommend AMFI to give more attention to their social goals in the enterprise wide and the institutions should establish suitable indicators to constantly monitor their progress towards the achievement of social goals. Furthermore, AMFI need to balance financial performance and social performance. In particular reference to the AMFI boards are should encouraged and appreciated the importance of social goals.

5.3.3 Commitment to assure social performance management

The link between risk management and social performance which has been the subject of this study has not yet been understood well enough in AMFI. AMFI need to pay close attention to social performance related risks like mission drift, reputation risk, employee dissatisfaction, and lack of transparency. In line with the Universal Standards for Social Performance Management, MFIs are encouraged to closely assess social performance related risks.

5.3.4 Developing of Management Information Systems (MIS)

GTZ (2000) show that an effective MIS is crucial in microfinance because of the large number of small value transactions conducted in microfinance. This could be not correctly reflecting loan tracking, inconsistencies of loan &account system data .MIS challenges were a problem faced by a lot of MFIs in the country. The same situation was happen the discussions we had with the management of the host institution revealed that the problem affected the whole microfinance sector in the country. According to discussion result made with managements the main reason for their failure to acquire a good MIS was financial constraint. Since AMFI manage a lot of borrowers we recommend that they invest in efficient information systems.

5.3.5 Liquidity risk management

The finding showed that liquidity risk management practices employed in the organization were inadequate. This could be, because of the absence of officer responsible to manage cash flow of the organization. Regarding to this, we appreciate AMFI to adopt comprehensive cash analysis procedures in order to assess and manage liquidity risk. This could be achieved through hiring qualified employ in the field.

5.3.6. Linking Internal Audit in social performance management

In line with the CERISE SPI Standards tools for Social Performance Management, we advise AMFI to make an effort to integrate social performance into the regular activities of their internal audit and risk management functions since internal audit divisions functions are limited to an accounting role, as was shown by Maitrot's (2014) study, MFIs tend to experience practice drifts and this may be manifested through malpractices like hard-selling of loans, harsh and abusive treatment of clients etc.

5.3.7 Cooperate with other microfinance institution

From the finding of the study AMFI well managed over indebtedness of its clients. To continue with previous appreciated performance we advice the institution to share client's loan profile with MFI this will enable AMFI to conduct necessary checks before lending.

5.3.8 Use of Risk Management to Improve Social Performance

This was the overall recommendation that can be made from this study, and we advice AMFI to adopt the use of risk management as a tool to improve social performance of the institutions. AMFI should be optimistic to employ effective risk management practices as this will benefit all their stakeholders, particularly clients, through better social performance.

5.4 Areas of further study

Future studies could investigate the role of system operation to ensure social performance management. Apparently, there is a considerable chance that AMFI may not be equipped to adopt internal operation system to managed to integrate social performance. Research could be undertaken to assess progress in this regard and also investigate the attitudes of management and staff towards this practice.

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A.APPENDIX -I: - A Questionnaire on Risk Management and Social Performance in AMFI Micro Finance Institutions. (To be filled by senior managers.)

Part –one; - general information

❖ **Instruction; - please encircle to indicate your personal details below: Note that the questionnaire is printed on both sides of the paper.**

1. Age; - 1. 18 - 25 years 2. 26 - 30 years 3. 31 - 35 year 4. 36 - 40 years 5. Over 40 years
2. Sex; - 1. Male 2. Female
3. How long has you worked in the microfinance sector?

   1. Less than one year 2.1 - 5 years 3. 6 -10 years 4. More than 10 years
4. Please encircle the highest educational qualification you achieved?

1. Certificate in Agriculture 2. Diploma in Accounting or Management 3. Degree in Accounting or Management 4. Master in Accounting or Management 5.Other

Part -two; -likert scale risk and social performance questions

- **Please tick the questionnaire below in the column (1-5) that best represents your opinion regarding the question asked.**

Note;- 1= Strongly disagree, 2= Disagree, 3= Neutral, 4= Agree, 5= Strongly agree

Q/N	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
5	Good repayment of loans protects AMFI from liquidity problems and It is a great opportunity For MFIs to be able to lend wealthier people.					
6	Good financial performance is a very important than social goals to be achieved by a MFI.					
7	Since AMFI now understand their clients very well, there is less need to conduct market research aimed At identifying the needs of clients					
8	Demographic factors like the trends in illnesses and deaths, educational levels, mobility of the Population have little effect on AMFI operations and business performance					
9	Over-indebtedness of clients is one of the major risks faced by AMFI.					
10	Political issues in a country have little effect on the operations of AMFI in the country.					
11	Macroeconomic factors like inflation and unemployment have significant effects on AMFI business Activities and affects relationships with clients					
12	One kind of operational risk AMFI could face is a poor MIS which does not Reflect correct loan Information					
13	It is acceptable for AMFI to occasionally use harsh and forceful methods to Recover debts from Clients					
14	There is strong competition between microfinance institutions operating in Ethiopia.					

15	Natural disasters like drought or floods could result in financial losses to a AMFI.					
16	There is less need to conduct customer satisfaction surveys since the opinion of clients regarding AMFI is reflected when they request for other loans or services					
17	There is nothing wrong with AMFI presenting interest rates for loans appear cheaper than they really Are, as long as this will help attract more clients.					
18	There is no need to check whether a client has loans from other financial Institutions before Granting them a loan					
19	The Board of Directors should be at the forefront of championing risk Management policies In AMFI.					

Part- three;-closed –ended risk related questions

❖ **Instruction; - please encircle the column that best represents your opinion regarding the question asked.**

Q/N	Statement	YES	NO	
20	Are AMFI loan officers required to conduct a thorough assessment of a client's ability to repay before disbursing a loan?			
21	Does AMFI have established procedures for clients to submit any complaints they may have and are such Procedures made known to all clients?			
22	Does AMFI occasionally check to ensure it is serving the market it intends to serve?			
23	Are AMFI loan officers required to check whether clients could have loans from other sources before disbursing loans to them?			
24	Does the risk management function in AMFI periodically produce any risk reports for the organization?			
25	Does AMFI train operations staff on acceptable debt collection practices and loan recovery procedures?			
26	Do the MIS used by AMFI produce reports related to problem/ delinquent loan portfolio performance?			
27	Do the MIS used by AMFI have the ability to track the performance of restructured loans separately?			
28	Does the AMFI MIS enable the segmentation and monitoring of loans into sub-portfolios e.g. by borrower Type, geography,			
29	Does AMFI have a clearly defined risk strategy that is set at the Board of Directors level?			
30	Does the Internal Audit function in AMFI check the quality of operations in branches, correct application of Credit policies and Process from origination to collection?			
31	Does AMFI 's Internal Audit or other monitoring systems check whether complaints made by clients have Been satisfactorily Resolved?			
32	Does AMFI's Internal Audit and/or other departments (except for Operations Department) visit a Representative sample of clients each year to monitor over indebtedness?			
33	Does AMFI ever conduct employee satisfaction surveys on an anonymous basis to allow employees to Communicate any grievances for improvement they could have?			
34	When setting target growth rates, does AMFI take into consideration the organization's internal capacity Including staff workloads and internal control capabilities?			
35	Does AMFI occasionally conduct surveys to assess client satisfaction and seek client feedback on Product design and delivery?			

Part –four; - open -ended risk related questions

- **Instruction; - Describe your feeling regarding the question asked below**

36. Please explain below the methods and tools used in AMFI to analyze Credit risk before disbursing a loan, if any.

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37) Does AMFI continue to review the individual credit risk of a borrower on a regular basis after the loan has been disbursed? If yes, please briefly explain the methodology used and frequency.

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38) Does AMFI conducts a Portfolio level credit risk review after disbursing loans? If yes, please briefly explain the methodology and frequency.

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39) Does AMFI execute Liquidity Risk Management/ Cash Management at the Branch Level? If yes, briefly explain the methods used. Who is responsible for that task? How is the work split between Head Office and Branch?

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40) Does AMFI continue to review the individual credit risk of a borrower on a regular basis after the loan has been disbursed? If yes, please briefly explain the methodology used and frequency.

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41) Does AMFI conducts a Portfolio level credit risk review after disbursing loans? If yes, please briefly explain the methodology and frequency.

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42) Does AMFI execute Liquidity Risk Management/ Cash Management at the Branch Level? If yes, briefly explain the methods used. Who is responsible for that task? How is the work split between Head Office and Branch?

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43) Does AMFI execute Liquidity Risk Management/ Cash Management at the Head Office Level? If yes, briefly explain the methods used. Who is responsible for that task?

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44) Please describe what happens to loans that are +1 day overdue until recovery or write-off. Please particularly identify "Soft" (early stages) and

"Hard" (late stages) of the collection processes:

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45) Please describes AMFI's loan loss provisioning policy.

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B. APPENDIX -II: A Questionnaire on Risk Management and Social Performance in Micro Finance Institutions (to be filled by Savings & Credit Officers)

Part –one; - General information

- **Instruction; - please encircle to indicate your personal details below.**

1. Age: 1. 18 - 25 years 2. 26 - 30 years 3. 31 - 35 yea 4. 36 - 40 years 5. Over 40 years
2. Sex: 1. Male 2. Female
3. How long have you worked in the microfinance sector?

1. Less than one year 2. 1 - 5 years 3. 6 - 10 years 3. More than 10 yea

4. Please state in full the highest educational qualification you hold?

1. Certificate in Agriculture 2.Diploma in Accounting and Management 3.Degree in Accounting or Management 4. Master in Accounting or Management 5. Other

Part-two; - closed-ended likert scale risk and social performance questions

❖ **Instruction; Please complete the questions by encircling in the column that best represents your opinion regarding the question asked. Note;-** 1= Strongly disagree, 2= Disagree, 3= Neutral, 4= Agree, 5= Strongly agree

Q/N	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
5	The most important objective for microfinance institutions is to meet their Financial targets rather than Social goals.					
6	It is not important to report poorly performing loans to management as this could result in unnecessary deterioration of the quality of a Savings & Credit Officer's portfolio and loss of promotion opportunities at work.					
7	Failure to serve clients in a polite and respectful manner could cause harm to the reputation of the microfinance institution.					
8	Using Harsh and forceful methods are important to recover debts from clients.					
9	There is no need to check whether a client has loans from other financial Institutions before granting them a loan.					
10	There is nothing wrong with AMFI finding ways to make interest rates for loans appear Lower or cheaper than they really are, as long as this will help get more clients.					
11	It is only the duty of Managers to make sure the organization is protected from financial losses. Savings & Credit officers have no role to play in this.					
12	Credit risk is the risk that clients may fail to repay the loans they would have taken.					

Q/N	Statement	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
13	It is important for AMFI to closely monitor macroeconomic factors like inflation and unemployment, as these could affect the institutions operation					
14	Over-indebtedness of clients is one of the major risks faced by AMFI and end up with Struggling repayment deadlines.					
15	Natural disasters like drought or floods could result in financial losses to a Microfinance institution.					
16	AMFI are exposed to a risk of loss arising from the dishonest acts of staff or clients who Could steal money from the institution.					
17	Staff working for AMFI holds positions of trust as they should not disclose to outsiders any Information about clients account.					

Part-three; - Closed- ended risk related questions

- **Instruction; Please completes questions below by ticking in the column that best represents your opinion**

Q/N	Statement	Yes	No	Not Sure
18	AMFI Savings & Credit officers are required to conduct a thorough assessment of a client's ability to repay Before disbursing a loan.			
19	Savings & Credit officers have a duty to prevent over-indebtedness of clients.			
20	Savings & Credit officers are required to clearly explain terms of all products to clients such as the total amount that The clients will repay.			

21	Savings & Credit officers are required to communicate with clients in such a manner that the clients understand the terms of the loan, their rights, and obligations.			
22	Clients are given adequate time to review the terms and conditions of the product and receive additional information Prior to signing contract.			
23	AMFI staff has received training on debt collection practices that are to be followed for clients.			
24	Savings & Credit officers are required to advise clients about their right to complain and how to submit a Complaint if a problem arises.			
25	As a Savings & Credit officer do you understand AMFI loan policies and procedures for rescheduling loans to clients?			
26	Is the number of clients you are responsible for as a Savings & Credit officer manageable to you i.e. is Your workload bearable?			
27	Have you ever had to use aggressive sales techniques or had to force clients to sign contracts.			

Part -four; - open ended risk related questions

- **Instruction; - Describe your feeling regarding the question asked below**

28 (a) Please list the three major risks that you think AMFI is exposed to:

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(b) Give reasons to justify why you think the risks you identified above are the major risks AMFI is exposed to.

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(c) What do you think AMFI should do in order to control the risks you identified above and reduce their effects on the organization?

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29) Please explain below the procedures or methods you use to judge whether a client has the ability to repay a loan before you disburse the loan.

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30) As a Savings & Credit officer do you continue to monitor the ability to repay of clients who would have taken loans after the loan has been disbursed? If yes, please briefly explain how this is done and how often the checks are done.

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31) You are approached by some women who would like to get a group loan from AMFI. From your judgment the business activities the women would like to use the money for do not seem very good and may not be successful. However, the women are willing to guarantee one another under group liability as is required by AMFI. Would you give a loan to the women? Please give reasons for your answer.

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32) You are approached by an individual who would like to get a individual loan that will be backed by physical collateral from AMFI. From your judgment the business activities the person would like to use the money for do not seem very good and may not be successful. However, the individual is willing to provide adequate physical collateral to back the loan. Would you give a loan to this person? Please give reasons for your answer.

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Declaration

I, the under signed, declare that this thesis is my original work, prepared under the guidance of D/r Getie Andualem. All sources of material used for the thesis have been dully Acknowledgement. It further confirms that has not been submitted either in part or full to any other higher learning institution for the purpose of learning any degree.

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Name Signature

St.Mary's University, Addis Ababa Ethiopia May 2016

Endorsement

This thesis has been submitted to st.mary's universities, school of graduate studies for examination with the approval as university advisor

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Advisor Signature